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In the Supreme Court of the United States

OCTOBER TERM, 1942

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

SABINE TRANSPORTATION COMPANY, INC.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

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The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit entered on June 30, 1942.

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 19–22) is unreported. The opinion of the Circuit Court of Appeals (R. 33–36) is reported at 128 F. (2d) 945.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 30, 1942. A petition for re-

hearing was filed on July 18, 1942 (within 21 days after entry of judgment, as required by the court's rules), and denied August 13, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

In 1937 taxpayer declared and paid a dividend in its own notes for the face amount of which it claimed and was allowed a credit in the computation of its undistributed profits tax for that year. Did Section 27 (a) (4) and 27 (e) of the Revenue Act of 1938 entitle the taxpayer to a second dividends paid credit with respect to the identical notes in 1938 when they were redeemed?

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved will be found in the Appendix, *infra*, pp. 6–9.

STATEMENT

The facts as stipulated (R. 10–19) were adopted by the Board of Tax Appeals as its findings (R. 19). They may be summarized as follows:

Taxpayer is a Delaware corporation with its principal office in Texas. It has only two stockholders. In 1937 it paid dividends of $30,000 in cash and $530,000 in its own ten-year 8 percent notes. For undistributed-profits-tax purposes, in its return for 1937 taxpayer claimed a dividends

paid credit of $641,562.60, consisting of the cash and also of the full face amount of the notes paid out as dividends, plus a dividend carry-over from the previous year. The Commissioner allowed this credit, but made adjustments in other items reported in the return, not here material, with a resulting deficiency in normal tax of $2,256.43 and in undistributed profits surtax of $117.40, to which taxpayer agreed. (R. 19–21.)

In 1938 taxpayer paid its two stockholders the full face amount of the dividend notes, and retired them. In its return for 1938 taxpayer claimed a second credit of the full face amount of these notes, this time under Section 27 (a) (4) of the 1938 act, dealing with amounts used to retire indebtedness incurred before the beginning of that year. The Commissioner disallowed the credit for 1938, and was sustained by the Board. (R. 21–22.) The taxpayer appealed, and the Circuit Court of Appeals reversed (R. 36).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

(1) In allowing the taxpayer a second credit upon the redemption of notes in 1938, which in 1937 when they were issued had been the occasion of a dividends paid credit equal to their full face amount.

(2) In reversing the decision of the Board of Tax Appeals.

REASON FOR GRANTING THE WRIT

As recognized by the court below (R. 34), its decision is in direct conflict with *Spokane Dry Goods Co.* v. *Commissioner,* 125 F. (2d) 865 (C. C. A. 9th). Also, the decision invalidates a reasonable administrative interpretation of the statute contained in Article 27 (a)–3 of Treasury Regulations 101.

The Government argued below that subsection (e) of Section 27 of the Revenue Act of 1938, which deals specifically with the credit allowable on the redemption of obligations previously issued in payment of dividends, controlled over the more general terms of subdivision (a) (4) of Section 27. The court below, however, gave effect only to the latter provision, which deals generally with the redemption of obligations, and denied effect both to the provision specifically dealing with redemptions of the type herein involved, and to the Treasury regulation. In conseqeunce the court below allowed a second credit in 1938 on account of an obligation which had already been the subject of a full credit in the previous year at the time of its issuance: an extraordinary result which alone might have suggested the view of congressional intent adopted in the regulation.

The Circuit Court of Appeals for the Ninth Circuit, on the other hand, took the view that the specific provisions of subsection (e) of Section 27

prevailed over the general terms of subdivision (a) (4) of Section 27, and upheld the regulation.

Though the issue cannot arise in the future under the existing revenue law, the question is nevertheless presented in a number of other cases pending in or which would go to circuit courts of appeals other than those which have already considered it.[1] Accordingly, the conflict should be resolved.

CONCLUSION

It is respectfully submitted that this petition should be granted.

CHARLES FAHY,
Solicitor General.

NOVEMBER 1942.

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[1] The following cases involving the question are pending on taxpayers' appeals in the Circuit Court of Appeals for the Seventh Circuit: *Journal Co.* v. *Commissioner*, 46 B. T. A. 841; *Jos. Schlitz Brewing Co.* v. *Commissioner*, decided April 30, 1942 (Prentice-Hall B. T. A. Memorandum Service, par. 42,239); *Winchester Repeating Arms Co.* v. *Commissioner*, decided August 28, 1941 (Prentice-Hall B. T. A. Memorandum Service, par. 41,404). The question has been decided for the Commissioner in *Noble Drilling Co.* v. *Jones*, by the District Court for the Western District of Oklahoma (decision rendered June 27, 1942, not officially reported but found in 1942 Prentice-Hall, par. 62879; motion for rehearing under consideration by the court). The question is pending in *Midland Broadcasting Co.* v. *United States*, awaiting trial in the District Court for the Western District of Missouri.

APPENDIX

Revenue Act of 1938, c. 289, 52 Stat. 447:

SEC. 13. TAX ON CORPORATIONS IN GENERAL.

(a) *Adjusted Net Income.*—For the purposes of this title the term "adjusted net income" means the net income minus the credit provided in section 26 (a), relating to interest on certain obligations of the United States and Government corporations.

(b) *Imposition of Tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation the net income of which is more than $25,000 (except a corporation subject to the tax imposed by section 14, section 231 (a), Supplement G, or Supplement Q) a tax computed under subsection (c) of this section or a tax computed under subsection (d) of this section, whichever tax is the lesser.

(c) *General Rule.*—The tax computed under this subsection shall be as follows:

(1) A tentative tax shall first be computed equal to 19 per centum of the adjusted net income.

(2) The tax shall be the tentative tax reduced by the sum of—

(A) 16½ per centum of the credit for dividends received provided in section 26 (b); and

(B) 2½ per centum of the dividends paid credit provided in section 27, but not to exceed 2½ per centum of the adjusted net income.

* * * * *

SEC. 27. CORPORATION DIVIDENDS PAID CREDIT.

(a) *Definition in General.*—As used in this title with respect to any taxable year the term "dividends paid credit" means the sum of:

(1) The basic surtax credit for such year, computed as provided in subsection (b);

* * * * *

(4) Amounts used or irrevocably set aside to pay or to retire indebtedness of any kind, if such amounts are reasonable with respect to the size and terms of such indebtedness. As used in this paragraph the term "indebtedness" means only an indebtedness of the corporation existing at the close of business on December 31, 1937, and evidenced by a bond, note, debenture, certificate of indebtedness, mortgage, or deed of trust, issued by the corporation and in existence at the close of business on December 31, 1937, or by a bill of exchange accepted by the corporation prior to, and in existence at, the close of business on such date. Where the indebtedness is for a principal sum, with interest, no credit shall be allowed under this paragraph for amounts used or set aside to pay such interest.

(b) *Basic Surtax Credit.*—As used in this title the term "basic surtax credit" means the sum of:

(1) The dividends paid during the taxable year, increased by the consent dividends credit provided in section 28, and reduced by the amount of the credit provided in section 26 (a), relating to interest on certain obligations of the United States and Government corporations;

* * * * *

(e) *Dividends in Obligations of the Corporation.*—If a dividend is paid in obligations of the corporation, the amount with respect thereto which shall be used in computing the basic surtax credit shall be the face value of the obligations, or their fair market value at the time of the payment, whichever is the lower. If the fair market value of any such dividend paid in any taxable year of the corporation beginning after December 31, 1935, is lower than the face value, then when the obligation is redeemed by the corporation in a taxable year of the corporation beginning after December 31, 1937, the excess of the amount for which redeemed over the fair market value at the time of the dividend payment (to the extent not allowable as a deduction in computing net income for any taxable year) shall be treated as a dividend paid in the taxable year in which the redemption occurs.

Treasury Regulations 101, promulgated under the Revenue Act of 1938:

ART. 27 (a)–3. *Amounts used or irrevocably set aside to pay or to retire indebtedness.*—(a) *Indebtedness.*—

* * * * * *

Double credits are not permitted, either for the same year or for separate years. Thus, amounts which have been or may be properly taken as a credit pursuant to section 27 (e) of the Act or section 27 (d) of the Revenue Act of 1936 (both sections relating to dividends in obligations of the corporation) may not again be included in the dividends paid credit under section 27 (a) (4) when the obligations are paid. No credit may be allowed under section 27 (a)

(4) for amounts used or irrevocably set aside to pay or retire indebtedness which represents an item which is allowable as a deduction from gross income, either for the same year or a different year. Thus the aggregate of the credits allowable under section 27 (a) (4) for amounts used or irrevocably set aside to pay or to retire obligations issued at a discount may not exceed the issue price of such obligations.

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